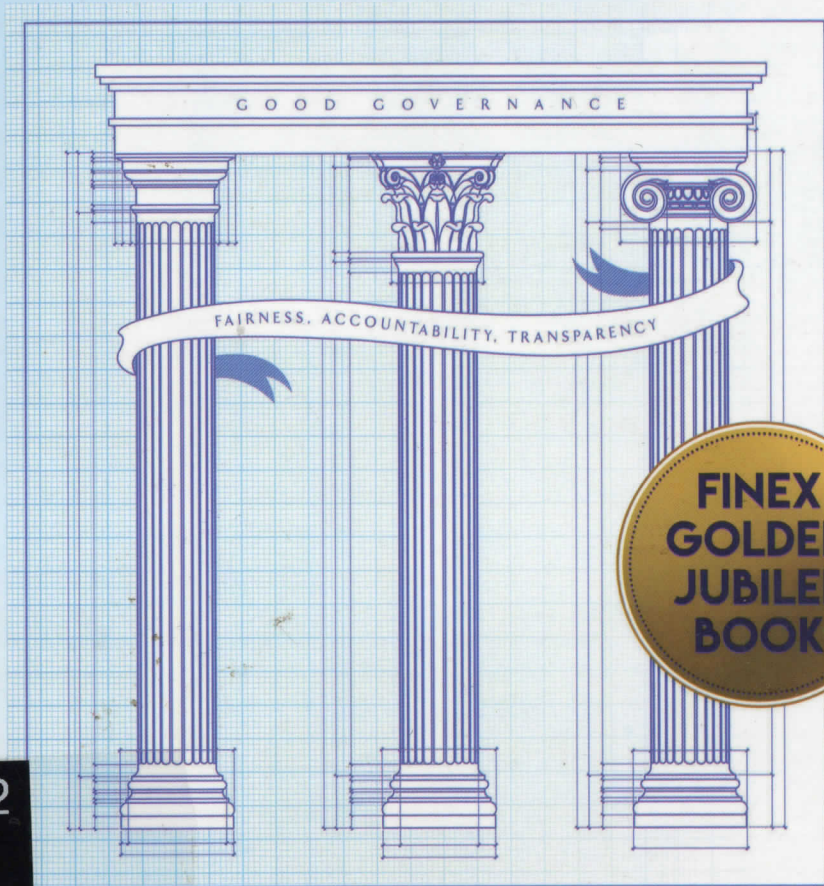




FINANCIAL EXECUTIVES INSTITUTE OF THE PHILIPPINES

PILLARS OF GOOD GOVERNANCE



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SONNY COLOMA





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PILLARS OF GOOD GOVERNANCE

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SONNY COLOMA



PILLARS OF GOOD GOVERNANCE

by Sonny Coloma

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Foreword

Good governance is a continuing journey. Good practices evolve over time. What stays constant is cooperation among all stakeholders in promoting and advocating good governance. In this regard, it is heartening to note that the Financial Executives Institute of the Philippines (FINEX) has unceasingly done its part. FINEX's continuing advocacy of good governance greatly contributes to the efforts of the Securities and Exchange Commission (SEC) to develop a globally competitive capital market and protect the investing public.

FINEX's publication of this book on corporate governance that is intended primarily for college and university teachers and students is proof of this advocacy. We commend FINEX for this initiative that will indubitably raise the level of financial literacy in the academe, while promoting greater awareness about the ever-rising standards in the quality of corporate governance. Cultivating good governance necessitates sowing seeds and there is no better ground to sow than in colleges and universities. After all, the students of today will be the business leaders of tomorrow. Inculcating in them core governance principles of fairness, accountability, transparency and responsibility is key to ensuring the continuous and fruitful journey of good governance.

We understand, too, that this book features the outstanding Chief Finance Officers (CFOs) that have been selected by FINEX in partnership with ING Bank N.V. Manila Branch for the past decade. Indeed, they represent the best and the brightest among the financial leaders

who are tasked with enhancing shareholder value and shepherding wealth creation efforts.

Another proof of FINEX's thrust to promote corporate governance is its active involvement in drafting the Code of Corporate Governance for Publicly-listed Companies (PLCs) that the SEC released in 2016. Using as key reference materials the G20/OECD Principles of Corporate Governance and the ASEAN Corporate Governance Scorecard, the Code seeks to elevate the corporate governance standards of Philippine corporations for enhanced global and regional competitiveness.

The Code is characterized by a "comply or explain" approach, which combines voluntary compliance with mandatory disclosure. Thus, publicly-listed companies must state their compliance with the Code provisions and explain any non-compliance. This approach also recognizes that there is no "one size fits all" in corporate governance since companies are given flexibility in determining their own corporate governance arrangements while also giving the market the power to determine whether these arrangements are indeed good practices. In this way, companies become accountable to their shareholders and the penalty for poor corporate governance is market-driven rather than regulator imposed.

Further, the Principle of Proportionality is applied to the provisions of the Code. This is to acknowledge the varying sizes and scope of corporate operations. The Code also encourages companies to adopt applicable best practices that they may have continuous improvement. This would ultimately benefit the investing public to be motivated to expand their participation in the flourishing capital market.

A year after the release of the Code, we are gratified to witness the robust growth of the country's capital market, highlighted by the attainment of record highs in the Philippine Stock Exchange Index (PSEI) and more importantly, the PLCs' increasing awareness and interest in practicing good corporate governance.

FOREWORD

As mentioned earlier, cooperation among stakeholders is essential and as FINEX marks its golden jubilee, we at the SEC look forward to many more years of cooperation and partnership in working toward a shared vision: a robust and inclusive Philippine capital market in the ASEAN and Asia-Pacific region.

TERESITA J. HERBOSA

Chairperson

Securities and Exchange Commission

Preface

In early 2017, the FINEX Board led by President Benedicta ‘Dick’ Du-Baladad decided to publish a book on corporate governance to mark the Institute’s golden jubilee in January 2018. As suggested by FINEX Past President Melito Salazar, this book will be disseminated widely to business professors and students of business in order to propagate a deeper appreciation of the role played by financial executives in enterprise management.

In retrospect, the groundwork for this book project began more than a decade ago. The initial idea was to underscore the role of chief finance officers (CFOs) as prime movers of good governance. In 2016, the annual search for CFO of the Year jointly undertaken by FINEX and the ING Bank N.V. Manila branch was themed, “The Decade of the CFO: Championing Good Governance.”

A closer look at the criteria used to select the CFO of the Year brings to the fore the significant influence of the Global CFO Study conducted by the International Association of Financial Executives Institutes (IAFEI) in 2005-2006 when its Chairperson was Dr. Conchita L. Manabat, FINEX Past President.

She recalls that there were five participating member institutes: Austria’s *Forum Finanzen-OPWZ*, Chinese Taiwan’s Finance Executives Institute, France’s *Association des Directeurs Financiers et de Controle de Gestion (DFCG)*, Germany’s *Die Gesellschaft für Finanzwirtschaft in der Unternehmensführung (GEFIU)*, and the Philippines’ FINEX.

This global project was launched on account of the recognition that the increasing complexity of the financial and capital markets, and the highly competitive and turbulent situation of the global economy had greatly influenced and redefined the CFO's roles.

When Dr. Manabat served as a resource person in the French Annual Financium in Paris, an event similar to the FINEX Week, she witnessed the honoring of the outstanding CFOs in different fields during the gala night. Hence, she broached the idea of launching a similar search for outstanding CFOs project to then FINEX President Abelardo 'Billy' Cortez, who eventually convinced ING Bank N.V. Manila Branch to be FINEX's partner. "The rest," says Dr. Manabat, "is history."

This book is entitled *Pillars of Good Governance* primarily to signify FINEX's staunch advocacy on continually adhering to the highest standards of ethical and socially beneficial practices in enterprise as well as public sector management.

The title also gives recognition to the vital role played by financial executives in upholding the principles of good corporate governance.

In 2007, *The Power to Govern*, a compendium of the Organization for Economic Cooperation and Development's (OECD) Principles of Corporate Governance, as well as several case studies on Philippine corporations and organizations, was published by the P&A Foundation, with Gregorio S. Navarro as editor. Greg Navarro was, at that time, the managing partner and CEO of Punongbayan & Araullo (P&A), the Philippine member of Grant Thornton International, and Chairman of the P&A Foundation. He went on to serve as FINEX President in 2010.

He acknowledged that this book grew out of a project of the FINEX good governance and ethics committee which he headed as chairman in 2005. He wrote: "At the time, Enron was the most studied, written-about corporate scandal; it was used to demonstrate how those in charge of governance failed in many ways and, together with Arthur Andersen, was the favorite whipping boy of many a lecturer on corpo-

rate shenanigans. The committee members were all sold on the need for local governance case studies and many volunteered to do the job.”

Significant progress has been made toward raising the level of general awareness and consciousness within the past decade following the publication of that first FINEX-inspired book on corporate governance. Hopefully, this second FINEX book will provide the momentum for even more rapid forward strides.

Chapter One discusses Why Good Governance Matters. The costs of deviating from the norms of good governance are high and the harmful consequences are pervasive. Over the past two decades, the specter of two major financial crises – the Asian crisis of 1997 and the Wall Street collapse of 2008 – continues to haunt corporate boardrooms and the highest echelons of government decision-making. After bearing the burden of being branded as “the sick man of Asia”, the Philippine economy has rebounded. A new trajectory of sustained growth has primed the country for shedding off its Third World status. Good governance is seen as the pivotal factor for this turnaround.

Chapter Two focuses on Institutions of Good Governance. The Organization for Economic Cooperation and Development (OECD), in partnership with the G20 countries representing the most advanced economies, has taken the lead in formulating guidelines and benchmarks for corporate governance that have gained universal acceptance. The Asian Corporate Governance Association has established similar baselines. The World Economic Forum’s competitiveness rankings are also seen as appropriate measures for assessing the state of corporate governance. In the Philippines, the Securities and Exchange Commission has exercised leadership in formulating a comprehensive blueprint for good corporate governance, including a five-year road map from 2015 to 2020 (see Annex One). In November 2016, the SEC further raised the bar of excellence by issuing Memorandum Circular 19, the Corporate Governance Code for Publicly-Listed Companies (see Annex Two).

Chapter Three is entitled CFOs: Stewards and Catalysts of Good Governance. The spotlight is beamed on the evolving role of the CFO and the competencies that are deemed vital in the exercise of the CFO function. The 2007 Deloitte study established the foundation for the CEO competency map that has been adopted by the IAFEI and its various affiliates. A survey of the perspectives of the ING-FINEX CFO of the Year awardees reflects broadly held views on the need for sustainability of governance practices as well as adherence to high ethical standards by leaders and executives of organizations.

Chapter Four is on CFOs of the Year: Exemplars of Good Governance. Each of the winners of FINEX-ING Bank's annual search is featured. Since 2007, twelve winners have been chosen, each of them truly outstanding and worthy of emulation. The selection of the CFO of the Year has become a much-awaited event, a testament to the prestige and respect accorded to those who have earned the recognition.

Chapter Five is about Personal Governance. Enlightened individuals who have attained a measure of personal mastery in terms of fulfilling their own personal vision and mission are primed to contribute significantly to building a culture of good governance. We round off this volume on corporate governance with a discussion on the role that up-and-coming potential leaders – popularly labeled as ‘millennials’ – may play in corporate and public sector boardrooms.

The field of corporate governance study awaits the participation of more dedicated researchers and practitioners. As FINEX marches on from its golden jubilee to its century year, new lessons and insights are likely to be learned. From its ranks will emerge many more outstanding financial executives who will ensure that enlightened advocates of good corporate governance lead progressive and socially responsible organizations.

Why Good Governance Matters

While risk-taking is a fundamental driving force in business and entrepreneurship, the cost of risk management failures is still often underestimated, both externally and internally, including the cost in terms of management time needed to rectify the situation. Corporate governance should therefore ensure that risks are understood, managed, and, when appropriate, communicated.

— ORGANIZATION OF ECONOMIC COOPERATION AND DEVELOPMENT

Instituting good corporate governance has become a priority item in the agenda of national governments and international multilateral organizations. Bank and business failures, as well as widespread financial crises with global impact, such as those that occurred in 1997 and 2008, have raised awareness about the canons of good governance and prudential risk management.

Good corporate governance matters. To govern means to conduct the affairs of a state, organization, or people.” The key concepts in the action word govern are: “control, influence, or regulate a person, action, or course of events.” Governance brings about order that allows people of diverse origins and persuasions to live in harmony. A stable government is able to rationally allocate both natural and human resources in ways that will engender economic growth. In corporations, business risks are mitigated by sound management practices that are informed by key principles such as fairness, accountability and transparency.

Good governance has eight key elements. According to the American Academy of Good Governance: “It is **participatory, consensus oriented, accountable, transparent, responsive, effective and efficient, equitable and inclusive, and follows the rule of law.** Good governance is responsive to the present and future needs of the organization, exercises prudence in policy-setting and decision-making, and ensures that the best interests of all stakeholders are taken into account.”

The impact of governance is pervasive as it affects the lives of people and the course of events at the global, national and community spheres.

Economist Daniel Kaufmann provides a comprehensive definition of governance as it applies to governments:

We define governance as the traditions and institutions by which authority in a country is exercised for the common good. This includes:

- ◆ *the process by which those in authority are selected, monitored, and replaced (the political dimension);*
- ◆ *the government’s capacity to effectively manage its resources and implement sound policies (the economic dimension); and*
- ◆ *the respect of citizens and the state for the country’s institutions (the institutional respect dimension).*

He also debunks popularly held myths, such as the following:

Myth #1: Definition: Governance and anti-corruption are one and the same.

He challenges the traditional definition of corruption as being “the abuse of public office for private gain,” pointing out that, from a wider perspective, “private agents also share responsibility, and where many acts which are not ethical (and thus may be regarded as corrupt) may

not necessarily be illegal.” Examples include the contributions made by private firms to political campaigns that eventually translate into undue influence when the beneficiary gets elected to public office, and “favoritism toward particular firms in the awarding of public procurement bids and contracts.”

Myth #2: Governance and corruption cannot be measured.

He cites six governance indicators used by the World Bank:

1. *Voice and accountability – measuring political, civil and human rights*
2. *Political instability and violence – measuring the likelihood of violent threats to, or changes in, government, including terrorism*
3. *Government effectiveness – measuring the competence of the bureaucracy and the quality of public service delivery*
4. *Regulatory burden – measuring the incidence of market-unfriendly policies*
5. *Rule of law – measuring the quality of contract enforcement, the police, and the courts, as well as the likelihood of crime and violence*
6. *Control of corruption – measuring the exercise of public power for private gain, including both petty and grand corruption, and state capture*

Myth #3: The importance of governance and anti-corruption efforts is overrated.

This is contradicted by increasing recognition that the quality of governance is a major factor in a country’s competitiveness. Global studies conducted by the World Economic Forum, Transparency International and the Institute for Management Development reflect a broad consensus among business and civil society leaders on the importance of raising the bar of governance in both the private and public sectors.

Global governance: OECD and G20

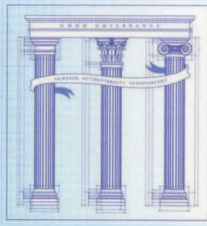
Over the past two decades, the quality of governance has come to the fore in light of the global financial meltdown in 2008 and the Asian crisis in 1997. David Korten, an American author and political activist proposed “an agenda for the new economy” on the eve of U.S. President Barack Obama’s inauguration in January 2009. He argued in favor of the return of the primacy of Main Street over Wall Street. He said that the money markets had tumbled out of control on account of the irresponsibility of bankers who made millions out of junk bonds and phantom financial instruments.

Here’s a capsule of Global Research’s analysis on “structural changes and deep-rooted contradictions” that triggered the crisis and produced dangerous fault lines in the governance of the global financial system:

The recent crisis is an expression of the structural changes and deep-rooted contradictions, which have occurred within the global system in the last 30 years. As a result, today’s global economic system is marked by three profound vulnerabilities: 1) the explosive growth of the financial system relative to manufacturing and the economy as a whole, and the proliferation of speculative and destabilizing financial instruments of wealth accumulation; 2) the loss of relative power by the US, and the rise of other centers of accumulation; 3) resource depletion and ecological crisis.

Declines of the real economy ensued, ushering in a period of stagnation and recession that hit the more advanced economies and inflicted higher poverty levels in less developed countries. This turmoil was characterized as the world’s worst economic downturn since the end of World War II.

These events were neither unexpected nor unprecedented. The Asian financial crisis of 1997, the collapse of the savings and loan in-



Good governance is a continuing journey. Good practices evolve over time. What stays constant is cooperation among all stakeholders in promoting and advocating good governance. It is heartening to note that...FINEX's continuing advocacy of good governance greatly contributes to the efforts of the Securities and Exchange Commission (SEC) to develop a globally competitive capital market and protect the investing public.

— excerpt from the foreword by **TERESITA J. HERBOSA**, SEC Chairperson

While risk-taking is a fundamental driving force in business and entrepreneurship, the cost of risk management failures is still often underestimated, both externally and internally, including the cost in terms of management time needed to rectify the situation. Corporate governance should therefore ensure that risks are understood, managed, and, when appropriate, communicated.

— ORGANIZATION OF ECONOMIC COOPERATION AND DEVELOPMENT

When one looks back at the past 50 years of the Philippines, the primary reason I think we have underperformed is the lack of good governance, both in the public — maybe primarily in the public—but also in the private sector. Now that we are being hailed as a resilient haven in Asia, one also cannot deny that governance is at the heart of the turnaround story we have been writing for the last five years.

— **CESAR V. PURISIMA**, Former Secretary of Finance



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